THE COST OF HOMEOWNERS INSURANCE

There are 2 major factors that determine how much insurance companies charge for homeowners insurance:

1. what are the chances of a loss and
2. how much will the insurance company have to pay out.

Almost all more specific factors can be grouped under 1 or the other major factor, and many will influence both. Since homeowners insurance also covers liability, other factors may affect the cost of insurance. For instance, according to a recent report, dog bites represent 1/3 of the claims under a homeowners policy. So, having a dog, especially a Chow, Doberman, German Shepherd, Pit Bull, Rottweiler, Wolf Hybrid, or mix of these will probably increase your premiums.

Factors Affecting the Chance of Loss

There are numerous factors that affect the chance of a loss.

The **construction** of a home is an important consideration. A house made of brick will be more fire resistant than one made of wood, and if there is a fire, there will probably be less damage to the brick house.

The **location** of the house also affects the chance of a loss. Certain locations are more prone to losses than others, so insurance company's rate different territories for underwriting risks. Those locations that have higher losses will be charged higher premiums.

Another factor related to location, but affects the amount of the loss more than the frequency, is the **fire-protection class** of the location. The **Insurance Services Office** (**ISO**), which provides information about underwriting risks to many insurance companies, rates territories from 1, which is best, to 10. Other factors related to fires are the distance of the home from the fire department and fire hydrants or other water supplies. For this reason, coverage in rural areas tends to be more expensive.

The **credit-based insurance score** is used by most insurance companies in rating risks for both home and auto insurance. Several studies by actuarial groups, notably **Tillinghast Towers-Perrin** and the **Casualty Actuarial Society**, have found, with a statistical correlation greater than 99%, that the **loss ratio**, which is the ratio of losses and associated expenses to premiums, is significantly higher for people with lower scores. In fact, for those with the lowest credit scores, the loss ratio actually exceeds 1, where losses exceed the premiums collected. A recent study by the Texas Department of Insurance showed that the loss ratio for homeowners with the worst scores was triple that of those with the highest scores.

Insurance scores depend on the credit history of a person. The **Comprehensive Loss Underwriting Exchange** (**CLUE**) **Report** is like a credit file on a house. The CLUE report is based on the claim history of the house. Insurers are using the CLUE report to drop or deny coverage based on a home's history of claims or damage reports. Used previously to find fraud and consumers who file numerous claims, insurers are now using this database to exclude greater risks, especially if a claim or even a report from the homeowner, indicates that the home may be susceptible to mold, water damage or flooding. The company *Checkpoint* gathers the information and maintains the database. The CLUE report lists the type and date of loss, and the amount for each claim for the past 5 years.

Factors Affecting the Amount the Payout

The insurance policy itself affects the amount of payout, including the **type of policy**, any **endorsements**, and the amount of the **deductible**.

The main difference between different types of policies is whether the coverage for the main residence is a **named-perils** policy or an **all-risk** policy, and which type of policy covers the other sections, like personal property. A **named-perils policy** covers only losses resulting from perils listed in the policy; an **all-risk policy** covers any risk unless it is specifically excluded. With a named-perils policy, the proof that a loss is covered rests on the insured; with an all-risks policy, the proof is on the insurer. Thus, an all-risk policy will command a higher premium than a named-perils policy.

A higher deductible will also reduce premiums. The standard deductible for most losses on a homeowner's policy is $250. Raising it to $1,000 or $2,000 can reduce the premium significantly—perhaps 25% or more. Raising it higher, however, will not reduce the premium proportionately.

Most endorsements add coverage to the standard policy, and therefore increase premiums.

Ways to Lower Your Premiums

If you have **multiple insurance policies**, ask each insurance provider what kind of deal you could get if you transferred all of your accounts to the one provider. Most insurance companies give discounts if you have more than 1 policy with them.

Some people try to save money by insuring less than the full value of their home, since a partial loss is far more likely than a complete loss. However, if your home is less than 80% insured, a **coinsurance penalty** will be applied that will reduce the amount of recovery that will be commensurate with the amount of underinsurance.

To reduce premiums, and to avoid the coinsurance penalty, you might want to insure, let's say, for 85% or more of its value, depending on how much risk you want to assume, and increase the amount every year by how much you think your property has increased.

Another way to reduce premiums is to improve your insurance score. Although insurance scores are calculated using the information in your credit file, only some of the information is used and it is weighted differently than the information used to calculate credit scores. Greater weight is given to payment history and total debt, and less for types of credit used or the number of inquiries made for loans and credit than in credit scores, for instance. Thus, lower debt and making timely payments will help to boost your insurance score.

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